

### Candax Energy Inc.

CAX : TSX : C\$0.75

**SPECULATIVE BUY**

**Target: C\$1.00 ↑**

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#### COMPANY STATISTICS:

52-week Range:	\$0.39-1.17
Avg. Daily Vol. (000):	337
Market Capitalization (M):	\$126.7
Shares Out. (M) basic:	168.9
Shares Out. (M) fd:	168.9
Net Debt (M):	(\$31,995.0)

#### EARNINGS SUMMARY:

FYE Dec	2004A	2005A	2006A	2007E	2008E
Equivalent Production (boe/d):	0	1,357	560	1,961	4,386
EPS:	(0.10)	(0.02)	(0.00)	0.01	0.02
Operating EPS:	(0.01)	(0.01)	(0.01)	0.01	0.02
P/Operating EPS:	(79.8x)	(51.5x)	(66.4x)	73.1x	47.8x
CFPS:	(0.10)	0.05	0.03	0.12	0.24
P/CF:	(7.8x)	14.5x	24.5x	6.4x	3.1x

#### SHARE PRICE PERFORMANCE:



#### COMPANY SUMMARY:

Candax Energy Inc. is an international energy company involved in oil and gas exploration and production and power generation. Candax has operations in Tunisia and looks to expand into the Middle East and other parts of North Africa. With an experienced, international oil and gas knowledgeable management team inclusive of Michael Wood, President and CEO, John Clarke, Executive Vice President and Chris Hopkins, CFO; Candax is primed for growth.

All amounts in C\$ unless otherwise noted.

### Energy -- Oil and Gas, Exploration and Production

## TURNING ON THE TAPS

#### Event – Good news from Ezzaouia field

Candax Energy announced surprisingly good results from its current workover program at the Ezzaouia field (31.4%). Current production from the field is in the range of gross 3,000 b/d, ahead of expectations and prior to the two-well infill program scheduled for H2/07. As a result, we are raising our production forecasts for both 2007 and 2008.

#### Impact - Positive

Production momentum has returned. Assuming a successful re-development at El Bibane (scheduled to commence drilling early July), we anticipate Q4/07E production could reach 3,320 bopd (excluding gas from El Bibane), compared to a Q2/07E average of 820 bopd. Moreover, full-year average 2008E production could climb by 6.9% to 3,550 bopd. We are decreasing our 2007 operating EPS (fd) to \$0.01 from \$0.02 and increasing our 2007 and 2008 operating CFPS (fd) estimates to \$0.12 and \$0.24 from \$0.11 and \$0.23, respectively.

#### Action

We are maintaining our SPECULATIVE BUY rating and raising our target price from C\$0.81 to C\$1.00.

#### Valuation

Our emphasis for our target price is shifting from a net asset value focus to a multiple of cash flow. We are making this change coincident with the expected rise in company production as a result of the recent news of better success at Ezzaouia and anticipated success at El Bibane. While execution risk remains, our target price of \$1.00 represents a conservative 4.2 times our forecast 2008 cash flow and 4.0 times on a debt-adjusted basis. Candax remains net debt-free with forecast working capital of \$25.5 million at year-end.

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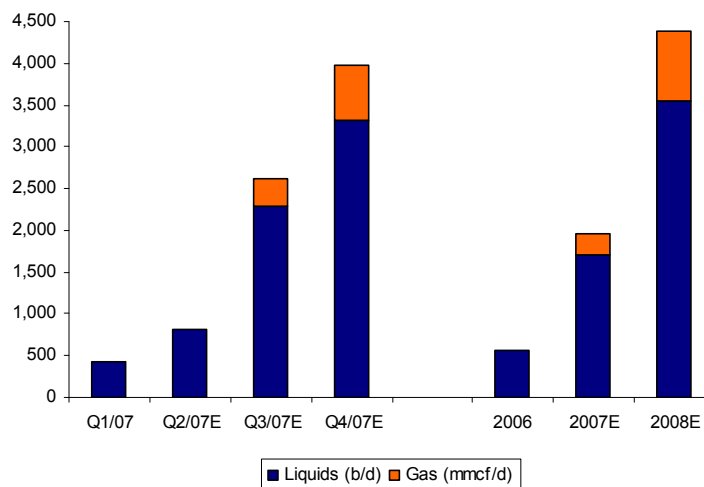
## TURNING ON THE TAPS

On June 5, 2007, Candax Energy announced that the ongoing workover program at the Ezzaouia field had been completed and that it resulted in a significant increase in production. This was a positive surprise and exceeded our expectations, with gross production increasing over threefold from 900 bopd to 3,000 bopd. Candax's net share (31.4%) of production of 1,100 bopd, from Ezzaouia, doubles its current production from all of its combined onshore fields in Tunisia.

As mentioned in our *Flash Update* of May 22, 2007, Candax has contracted the West Titania jack-up drilling rig with Seadrill which is in the process of being towed, currently off the coast of Morocco, to the El Bibane field in Tunisia. The rig is expected to be fully mobilized by the end of June with drilling operations expected to commence early July, post-mobilization, and initial production starting during mid-Q3/07.

Starting during the third quarter and beyond, incremental production from the El Bibane field and well workovers at Ezzaouia are expected to provide Candax with a steady stream of higher cash flow. Most of the incremental cash flow impact is consistent with multiple inventory liftings planned during H2/07 and beyond. See Figure 1 for our forecast of Candax's average daily production for 2007 and 2008.

**Figure 1: Candax's average daily production**



Source: Company reports, Canaccord Adams estimates

### Revisiting our estimates

As a result of the unexpected positive workover results from Ezzaouia, we have updated our 2007 and 2008 production outlook and estimates. We now expect production in 2007 and 2008 to increase to 1,700 bopd and 3,550 bopd from 1,350 bopd and 3,200 bopd, respectively. We are decreasing our 2007 operating EPS (fd) estimate to \$0.01 from \$0.02 and increasing our 2007 and 2008 operating CFPS (fd) estimates to \$0.12 and \$0.24 from \$0.11 and \$0.23, respectively. See Figure 2 for more information on the company's operating and financial results and our estimates.

7 June 2007

**Figure 2: Operating and financial and forecast summary**

	Q1/07	Q2/07E	Q3/07E	Q4/07E	2007E Old	2007E New	2008E Old	2008E New
Net Income	(877)	(658)	1,147	2,121	2,906	1,734	2,720	2,703
<b>Reported EPS (FD)</b>	<b>-0.01</b>	<b>0.00</b>	<b>0.01</b>	<b>0.01</b>	<b>0.02</b>	<b>0.01</b>	<b>0.02</b>	<b>0.02</b>
<b>Operating EPS (FD)</b>	<b>-0.01</b>	<b>0.00</b>	<b>0.01</b>	<b>0.01</b>	<b>0.02</b>	<b>0.01</b>	<b>0.02</b>	<b>0.02</b>
Cash Flow	369	1,198	6,943	11,144	17,847	19,654	39,158	41,781
<b>CFPS (FD)</b>	<b>0.00</b>	<b>0.01</b>	<b>0.04</b>	<b>0.07</b>	<b>0.11</b>	<b>0.12</b>	<b>0.23</b>	<b>0.24</b>
Net Capital Spending	(2,120)	(10,000)	(8,000)	(9,280)	(29,400)	(29,400)	(30,000)	(30,000)
Net Debt/(cash) incl. Working capital	(31,995)	(23,193)	(22,136)	(24,000)	(22,485)	(24,293)	(31,643)	(36,074)
Liquids (b/d)	420	822	2,283	3,317	1,355	1,711	3,210	3,553
Gas (mmcf/d)	0	0	2	4	2	2	5	5
<b>Equivalent (boe/d)</b>	<b>420</b>	<b>822</b>	<b>2,617</b>	<b>3,984</b>	<b>1,688</b>	<b>1,961</b>	<b>4,043</b>	<b>4,386</b>

Note: Actual timing of the oil inventory liftings may vary from our expectations and may have an impact on cash flow.

Source: Company reports, Canaccord Adams estimates

### Shifting our valuation focus

With Candax's growing production and cash flow, we are shifting our target price emphasis from a net asset value focus to a multiple of cash flow. Candax shares previously received support from its strong net cash position and value of its proven and probable oil and gas reserves. This year is aimed at accelerating and maximizing the value of its oil and gas assets through a workover and in-fill program at Ezzaouia and a redevelopment of the El Bibane field, the results of which were expected to generate both higher production and cash flow. The early results from Ezzaouia are positive and while risk remains, we anticipate the El Bibane field development should commence in Q3/07.

Candax shares have rallied up to \$0.75 in the last couple of days and are trading at 3.1 times our new 2008 cash flow estimate. With some execution risk remaining, we are using a conservative target of 4.0 times 2008E debt-adjusted cash flow, equating to our \$1.00 target price. We believe that as quarterly production and cash flow momentum builds, the market will also adopt a similar approach.

### Summary and conclusion

After a trying start for Candax, it appears the company is now getting some positive news with the recent well results at Ezzaouia. Moreover, the arrival of the West Titania jack-up drilling rig in late June and the commencement of the redevelopment at El Bibane is expected to contribute significantly to results in late 2007 and into 2008. In this regard, the Candax story is unchanged. The company's financial position remains strong, and operations are starting to turn the corner with strong gains now anticipated in 2007 and 2008. In our view, the possibility exists for a return to the Chaal prospect as well as the deep Triassic at Ezzaouia, either of which offer potential significant upside. In addition, Candax continues to pursue other investment opportunities in and around its core focus areas in North Africa/Middle East. We believe Candax shares are relatively inexpensive and are maintaining our SPECULATIVE BUY rating and increasing our target price from C\$0.81 to C\$1.00.

**Investment risks**

In addition to operating risks inherent in oil and gas exploration and production activities, oil and natural gas price realizations and production may be lower or higher than our forecasts. Collectively, these risks could impact the company's valuation and our forecasts.

Candax acquired producing assets that are mature with a relatively short reserve life and a high water cut. There is no guarantee that all future volumes of production will occur in sufficient quantities to make existing fields commercial. Two major fields (El Bibane and Ezzaouia) currently represent greater than 95% of the proved value of Candax. Should either of these fields experience a production-related problem for a prolonged period of time, there could be a material impact on our financial and valuation estimates. Unless new discoveries or assets are acquired, future cash flows from existing assets will decline substantially, which may impact the future valuation of Candax. All producing and potential properties are presently located in Tunisia. Although currently seen as a relatively stable government, the company's operations, financial results, and valuation could be adversely affected by events beyond its control taken by the current or future governments with respect to policy changes regarding taxation, regulation, and other business environment changes.

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**Site Visit:**

An analyst has visited the issuers' material operations in Tunisia and corporate headquarters in Toronto. No payment or reimbursement was received from the issuers for the related travel costs.

**Price Chart:\***



Date	Analyst	Rating	Target Price
1) 09/22/05	TP	Speculative Buy	1.50
2) 09/26/05	TP	Speculative Buy	0.83
3) 04/04/06	TP	Speculative Buy	1.33
4) 10/04/06	TP	Speculative Buy	0.88
5) 03/06/07	TP	Speculative Buy	0.78

\* Price charts assume event 1 indicates initiation of coverage or the beginning of the measurement period.

**Distribution of Ratings:**

Global Stock Ratings  
(as of 1 May 2007)

Rating	Coverage Universe		IB Clients
	#	%	%
Buy	310	58.5%	41.9%
Speculative Buy	64	12.1%	71.9%
Hold	132	24.9%	34.1%
Sell	24	4.5%	4.2%
	530	100.0%	

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Company	Disclosure
Candax Energy Inc.	1A, 2, 3, 7, 11 (John Zaozirny)

7 June 2007

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